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A free newsletter to the sectional title industry by Tertius Maree Associates

SECTIONAL TITLE SCHEMES: THE REAL VALUE OF GOOD GOVERNANCE

The market values of sectional title units are determined not only by the condition of bricks and mortar or the attractiveness of the accommodation, but importantly, also by the quality of management. For this reason a prospective buyer should look at much more than merely the superficial aspects before committing to a purchase.

Sight must not be lost of the fact that ownership of a sectional title unit is somewhat more complex than ownership of an ordinary house and that different and more complex standards of assessment apply. Apart from the fact that a prospective buyer must be aware that he or she will become a member of a community bound by rules and managed by an elected board of trustees, it should be understood that a good grasp of sectional title administration and sound governance by members are basic requirements in order to enhance and preserve value. Because trustees are elected from the general pool of owners, it is important that all owners should be at least acquainted with the basics of sectional title management. New owners usually do not have sufficient knowledge of sectional title affairs and simply assume that appropriate management structures are in place and that management is being conducted at an appropriate level. This is often not the case.

Prospective buyers must understand that the quality of management will have a direct impact upon their Rands and Cents, and such standards will vary from one scheme to the next. What are the signs of good or poor management which a prospective buyer should look out for? What follows are a few markers, in no particular order:

- Find out who the managing agent is and conduct an interview with him/her. Obtain his/her views on the standard of management but do not accept such views unreservedly.
- Enquire about any unresolved disputes - a bad marker.
- Find out whether a substantial number of units are being let - often a warning sign.
- Obtain a copy of the management and conduct rules from the managing agent. If he/she cannot provide copies, be worried. Check the contents of the rules or have an attorney check them. Pay particular attention to provisions about pets - an aspect which leads to many disputes in sectional title schemes. Make sure that any parking arrangements which you may require are provided for.
- Also obtain a copy of the sectional plan from the managing agent. Again, be very concerned if he/she does not have a copy. The sectional plan will show the layout of

all the sections and their respective participation quotas according to which, amongst other things, the proportions by which owners must contribute to the levy fund are determined. It may also indicate the existence of exclusive use areas, although these may also have been established in the rules. Make sure that any exclusive use area described in your deed of sale is accounted for in the sectional plan or the rules.

- Be careful about buying into small schemes, i.e. schemes of less than about six units. Avoid buying into schemes consisting of only two or three units. Disputes in such units are almost guaranteed and owners in such schemes tend to ignore the rules and statutory requirements.
- Obtain copies of the financial statements, budget, and insurance schedules and consider same. Obtain advice if necessary.
- Ask the managing agent for information about arrear levies. Although detailed information cannot be expected, you should be able to gauge whether this is a problem. Remember that levies not paid by some owners place a financial burden on others. If the percentage of arrears is more than 10%, be forewarned. Enquire whether the body corporate has STILUS insurance cover for unpaid levies, in which case the arrears would not be a concern.
- Enquire as to the existence and level of a reserve fund. This is a good indicator of the standard of governance. Poorly managed schemes make no provision for future or unforeseen expenses for the short-term benefit of keeping levies at a low level. Remember that when buying your unit you are also buying a portion of the reserve fund and you need to know whether you are getting your money's worth.
- Ask the managing agent whether any special levy has recently been imposed or if such levy is under consideration. The need for a special levy usually arises when no proper provision has been made for periodic maintenance work by building up a reserve fund.
- Check the condition of the common property. If it is poorly maintained you can be assured that a substantial special levy is to follow in the near future, or that the market value of your intended unit is on a slippery slope, or both.
- Find out whether annual general meetings are being held regularly and, if possible, obtain a copy of the minutes of the last one held.

Owners should understand that all of them, including the trustees, are in the same boat and that good governance is a team effort and which, ultimately, is conducted by the owners themselves. They have, after all, elected the trustees, may dismiss them, and have been provided with effective statutory tools to ensure that their boat is being steered towards safe waters.

Owners simply cannot afford the luxury of non-involvement in the affairs of their scheme.

Tertius Maree

LEVY DETERMINATION: CHECKLIST FOR TRUSTEES

Trustees should ensure that the following things are in place for determination and legal recoverability of ordinary levies, increased levies, special levies and additional levies:

CHECKLIST FOR ORDINARY LEVIES

- Members' resolution (ordinary majority resolution) at AGM to approve budget (with or without changes) for the financial year.
- Trustees' resolution to apportion the approved budget to the units per the participation quotas (or other prescribed formula) and to determine the installments. In addition the trustees could consider qualifying their resolution to the effect that in the event of default by an owner his/her levies for of the remainder of the financial year will become immediately due and payable. *See the example of trustees' resolution below.* The resolution should incorporate a schedule.
- Written notice to owners of the amount due which should be sent to owners within 14 days after the AGM, preferably incorporating a statement of the levies due.
- Trustees' resolution to determine the interest rate to be charged in respect of arrear levies. *See example below.* This could be incorporated in the resolution for the levies.

CHECKLIST FOR SPECIAL LEVIES

- Trustees' resolution to apportion the amount required according to participation quotas of sections (or other prescribed formula) and to determine whether payable in one sum or in installments.
- Written notice to owners of the amount due. (Statement)

CHECKLIST FOR INCREASED 'INTERIM' LEVIES AFTER FINANCIAL YEAR END

- Trustees' resolution to determine the percentage increase (up to a maximum of 10%) of the ordinary levies.
- Written notice to owners of amount due. (Statement)

CHECKLIST FOR ADDITIONAL LEVIES (EXCLUSIVE USE AREAS)

- Members' resolution (ordinary majority resolution) to approve the budget for the ensuing financial year at the annual general meeting, which budget should make provision for the expenses relating to exclusive use areas.
- Trustees' resolution to apportion the budgeted amount in respect of exclusive use areas to the owners of such areas in accordance with the (estimated) expenses for each exclusive use area. *See the example of the trustees' resolution below.*
- Notice to the owners of the additional levies due in respect of the financial year. (This should be incorporated with the notice and statement for ordinary levies).

(EXAMPLE OF TRUSTEES' RESOLUTION)

THE BODY CORPORATE OF THE ABC[1] SECTIONAL TITLE SCHEME SS No. 123/2001[2]

TRUSTEES' RESOLUTION

to determine ordinary levies and additional levies in respect of exclusive use areas in terms of section 37(2) of the Act, and to determine the interest rate in respect of arrear levies in terms of management rule 31(6)

PASSED AT A TRUSTEES' MEETING HELD AT * ON * 2012[3]

WHEREAS the Budget of the body corporate for the financial year commencing on 1 March 2012[4], as contemplated in Management Rule 36(1) and (2), was duly approved by the members at an annual general meeting of the Body Corporate held at Cape Town on the 30th of December 2011[5], as appears from the minutes of the said meeting;

ACCORDINGLY, and in compliance with section 37(2) of the Sectional Titles Act, the trustees hereby resolve that the estimated expenses of the Body Corporate as determined in terms of the Budget be apportioned to owners of sections and in respect of exclusive use areas, as appears from the attached Schedule marked "A.[6]

The ordinary levies and additional levies, as indicated in Schedule A, will be due by owners in equal monthly installments, payable monthly in advance on or before the 1st day of each month of the financial year.[7]

The trustees further resolve that if an owner fails to pay his levies or any other amounts to the body corporate on the date it is due-

(a) the owner shall be liable for interest to the body corporate at an interest rate of X %[8] (X per cent) per annum compounded monthly, calculated from the due date until date of payment, both days inclusive; and

(b) all levies due by the owner in respect of the remainder of the financial year shall become immediately due and payable to the body corporate in one amount .

TRUSTEE TRUSTEE

Ilse Kotze

[1] Insert name of the scheme.
[2] Insert SS number of the scheme.
[3] Insert place and date of Trustees' meeting or alternatively date on which the resolution was adopted in writing.
[4] Insert date on which financial year commences.
[5] Insert place and date of annual general meeting.
[6] Attach a schedule containing names of owners, section numbers, participation quotas, exclusive use area numbers, ordinary levies and additional levies payable.
[7] Insert the installments in which levies are payable.
[8] Insert the rate of interest in respect of arrear levies.

END OF THE TRI-PARTITE AGREEMENT?

One may think that the collection of arrear levies is a simple and straightforward legal process whereby a body corporate is 'guaranteed' payment of outstanding levies. When in default, the unit is attached, sold in execution and the proceeds used to settle the arrears. In practice however, it is never that simple. Show me any collection matter and there is a distinct possibility that I will be able to find something wrong, or at least something that may give an opposing party some ammunition.

One thorny aspect to consider when dealing with an owner who is in arrear, is the proper issue of a levy clearance certificate when the unit is sold. [A levy clearance certificate may be described as a document by which the body corporate certifies the outstanding amount due by an owner before a unit may be transferred]. The certificate is issued by either the managing agent or the trustees to the conveyancer prior to transfer of the unit.

Owners become liable for the payment of ordinary levies on the date when the trustees determine the individual levies by means of a trustees' resolution. This should take place at the first trustees' meeting after approval of the budget by the members at the AGM. The trustees' resolution is usually made by way of acceptance of a levy schedule listing the owners, section numbers, participation quotas and monthly levies. Prior to the amendment of section 37(2) of the Act in June 2010, registered owners of units as at the time of the trustees' resolution were liable for ordinary monthly levies for the duration of the financial year. If a new owner bought a unit during the course of the financial year he would not be automatically liable and to protect the interests of the body corporate two options were available -

(1) Procure payment in full of outstanding levies for the balance of the year; or

(2) Conclude a tri-partite agreement between seller, purchaser and the body corporate in terms whereof the purchaser assumes responsibility for the payment of remaining levies as from the date of registration of transfer.

In terms of the abovementioned amendment to section 37(2) a new owner becomes liable for payment of the ordinary levies automatically as from date of transfer of the unit. A tri-partite agreement has therefore become defunct.

Or has it?

In terms of section 37(2A) a special contribution (special levy) becomes due on the passing of a resolution of the trustees and is recoverable from persons who were owners of units at the time when the resolution was passed.

It is important to distinguish between ordinary monthly levies and special levies, and this distinction should be borne in mind when a levy clearance is issued. Section 37(2A) does not contain a similar proviso as in section 37(2) that a new owner assumes responsibility for continuation of payment of a special levy automatically.

It often happens that special levies are imposed for large amounts, such as for major renovations of the building. If the individual special levy contributions are large, trustees sometimes determine that it is payable in monthly instalments, for example 6 equal monthly instalments. What happens now if, after the special levy was imposed by the trustees, the owner sells his unit? It is clear that the situation is different from the case of ordinary levies and the new owner will not be liable for continuation of payments or payment of any arrears without some interceding arrangement.

When a levy clearance is to be issued it is therefore essential that any unpaid special levy be dealt with appropriately. If the special levy or any balance thereof is to be paid by the seller, it must first be paid in full or an undertaking must be obtained by the conveyancer. If the purchaser is to pay the balance or to continue payment of instalments it is necessary to obtain a tri-partite agreement in order to secure payment.

No, the tri-partite agreement is not yet dead and should be utilised whenever the purchaser of a unit is required to take over responsibilities of the seller in respect of any outstanding special levies.

Jacques Maree

SOLIDATUS REVISITED

The decision in Solidatus Body Corporate v De Waal and Others was delivered in the old Transvaal Provincial Division of the Supreme Court in May 1997. It was one of the earlier reported High Court decisions about sectional titles and remains one of the most controversial. Although it is a provincial decision and as such serves as a precedent only in the area of the former Transvaal Provincial Division, it has had an enduring and unfortunate impact upon sectional title administration in all provinces.

The Solidatus building consisted of sixty apartments, including eight sections with patios and eight with balconies, which were exclusive use areas. Soon after construction these started leaking and, not unusually, damages could not be claimed from the developer who had been liquidated. In order to effect the necessary repairs, additional levies were raised against the owners with the patios and balconies. These owners refused to pay, arguing that due to the fact that work related to building defects, it should not be categorised as 'maintenance.' They felt that the costs of repair should be apportioned to all owners according to their participation quotas. The parties agreed to apply to the High Court for a declaratory order.

[An incidental but important issue appearing from the report was that the members at a general meeting had by majority vote 'authorised' the trustees to raise a special levy upon the owners with exclusive use balconies and patios. In terms of the Act the authority to determine and raise levies are vested in the trustees and only the trustees. The reason for this is evident from the facts of Solidatus where the minority with exclusive use areas were outvoted by the majority at the general meeting].

During the hearing the Court, probably having been misled by the issues put before it, focussed on the question of what constitutes maintenance: whether replacement also qualifies as maintenance even if such replacement includes an element of betterment, and whether repair of building defects also qualify as maintenance. The conclusion that it reached that 'maintenance' includes such functions is a useful one, but it did not address the true question which I put as follows in an article published shortly after publication of the report:

> *Must owners with exclusive use areas (or sections) be held responsible for the costs of repair (maintenance) of construction defects which affect the structural integrity of a building and accordingly also affects other owners?*

Put in this way it seems evident, to me at least, that the answer should be that such costs should be borne by all owners according to their participation quotas and that a special levy should be raised against all owners if reserves are insufficient.

The report did not mention, but at the time I suspected, that the patios may actually have formed a roof of a parking garage or something similar underneath. To my mind this would have been a crucial factor as the leakage into the parking garage would actually have been the nub of the problem, which should have affected a ruling as to owners' obligations.

The Court spent abundant time on the question whether an owner is liable for the costs of maintenance of his exclusive use area. This is clearly so according to the wording of section 37(1)(b) which indicates that whereas the duty to perform maintenance rests with the trustees, the particular owner is liable for 'additional levies' in order to defray the costs of such maintenance. But this still does not answer the question about maintenance to common structural items such as a weight-bearing column or wall, or, as in the Solidatus case, a structural slab forming a roof to what is underneath.

Subsequent to my 1997 article I received a letter which, freely translated and summarised, read as follows:

> *In 1997 I was an owner of one of the Solidatus apartments with the patios in question. It was indeed so that the patios formed the roof of a parking garage underneath. The trustees, pressurised by the majority, sought to defray the costs of repair upon the owners with patios.*
>
> *After the judgment the respondent-owners gave notice to appeal. After further consideration, and due to the expected costs of an appeal, the trustees convinced the members to accept a compromise deviating substantially from the court decision. A substantial increase of the general levies was imposed on all members to fund the repairs which were then satisfactorily executed.*

I always illustrate my view about maintenance to a structural item with 'the little old lady' with a weight-bearing column inside her section in a high-rise building. Is she obliged, or even entitled, to repair structural cracks in the column merely because it is situated inside her section?

Tertius Maree

THE NEW COMPANIES ACT AND HOMEOWNERS' ASSOCIATIONS

The new Companies Act No 71 of 2008 came into being on 1st May 2011. The rationale for revision of the Act was to incorporate current international best practices in conjunction with current South African legislation. This article will be divided in two parts where the first part will provide a brief synopsis of the impact of the new Act on pre-existing Homeowners' Associations, the second part, also to be published in MCS Courier, will look in more detail at certain applicable provisions.

A homeowners' association (HOA) is a development scheme consisting of residential and/or commercial units (erven) established on a piece of subdivided land. Upon application by a developer to subdivide the land, a condition is imposed by the local authority in terms whereof the owners of erven within the subdivision are compelled to become members of more HOA governed by a constitution. Homeowners' associations consist of two types, namely associations created in terms of the Companies Act or common more associations. Due to the influence of the Land Use Planning Ordinance of the previous Cape Province, common more associations are more popular in that region but both formats could be used in all regions.

When the company format was preferred, it was in the past mostly done as a non-profit association commonly known as a Section 21 Company.

As from 1st of May 2011 all non-profit companies established under the old Act are being considered to be non-profit companies under the new Act. These 'old' companies were incorporated with more than one founding document, usually a memorandum of association and articles. These documents will now be merged into one, known as the Memorandum of Incorporation (MOI).

The first apparent requirement for a HOA established under the old Act is to amend its founding documents to comply with the naming requirements under the new Act. Gone is the 'association not for gain' as part of the name, to be replaced by the acronym 'NPC' which stands for 'non-profit company'. There is a further acronym which must be included and dealt with later herein.

The articles of association were generally known as the constitution of a section 21 HOA which provides for the duties and responsibilities of members and directors, the holding of meetings, voting rights, etc. The provisions of the articles of association remain in force even if they are inconsistent with the provisions of the new Act but must be brought in line within a period of two years (before 1 May 2013) after commencement of the Act. There is, however, a qualification to this in that any conflict in the articles will be void if it relates to any of the following:

(1) Directors duties, conduct and liability;

(2) Members' rights to receive notice or have access to information; or

(3) Directors' and members' meetings and the adoption of resolutions.

Should there be a conflict, the provisions of the new Act apply.

The Act stipulates that certain provisions of the MOI may not be changed. These provisions will be dealt with more extensively in my subsequent article in MCS Courier. There are however numerous provisions that can be amended, either at establishment or subsequently such as:

(1) The requirements to amend the MOI;

(2) Rights relating to proxies;

(3) Obtaining of finance by the HOA;

(4) Notice requirements of meetings;

(5) Quorum requirements; and

(6) Voting requirements for resolutions obtained at members' meetings.

The new Act makes provision for the incorporation of special conditions or the prohibition to change certain of the provisions of its MOI. These companies are known as 'ring fenced' companies. Such companies must have the additional abbreviation 'RF' added to its name. This will apply to all HOA's where the local authority has imposed conditions for the development such as that owners are compelled to belong to the HOA. Such provisions may never be altered by the members. An example of a HOA's name under the new Act is: Winelands Homeowners' Association (RF) NPC.

Directors of HOA's established under section 21 of the old Act have their work cut out with regards to compliance with the provision of the new Act. The name of the HOA must be changed and the articles of association must be brought in line before 1st May 2013.

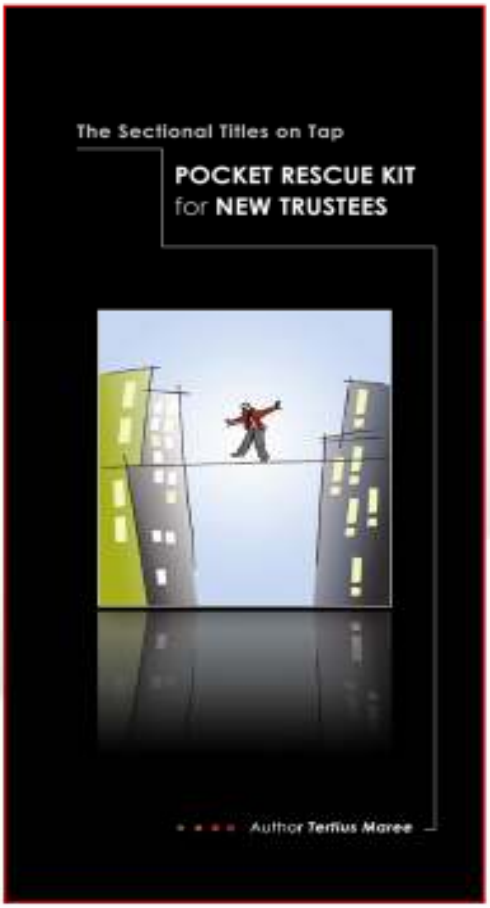
The new Act has introduced various advantageous provisions. Administration of the company and association expenses have been streamlined, higher standards are set for corporate governance and the fiduciary responsibilities of directors are much stricter. Access to and disclosure of information is more regulated. All in all it appears that the new Act is much more in tune with the current requirements of present day companies.

Jacques Maree

[With acknowledgement to the excellent course on home owners' associations presented by Prof. Graham Paddock]

BOOK LAUNCH!

This is the must-have for all new trustees.



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PREPAID WATER METERS HAVE ARRIVED!

(Advertorial)

For many years we've had the advantage of prepaid electricity meters, firstly on an optional basis and then it became compulsory for all new homes. Due to its success everybody has been wondering when prepaid water meters would become available, water usually being the biggest item in the budget and very prone to skewing when apportioned as part of the levies. An good example is the little old lady living on her own in the biggest flat in the building (with the biggest PQ) compared to a 2 roomed flat which is overcrowded with 6 people in it. She will be paying a totally disproportionate amount towards the water, which is unfair.

Whilst water meters have been on the market for some time, they were always complicated and very expensive. With new technology available today an innovative new prepaid water meter is now available to all property owners.

This is a 'must have' for bodies corporate to –

- exclude the risk of non-payment of levies (including water);
- substantially improve cash flow from the current arrears billing system to pre-paid; and

- put the burden of consumption on the person who is actually using/wasting water rather than including it in the budget and sharing it on the PQ method.

Trustees must advise their members under PMR 33.2 that they are fitting them, how they will benefit the members and how it will be paid for. (Cash, special levy or financed).

Each member will be entitled to the normal free water allocation as well as the allowance for sewerage. This dual recovery of charges to members is highly effective and leaves the body corporate to pay only the refuse charge on their municipal account.

It should be noted that there are bodies corporate that still only receive 6kl free water although there may be 100 units in the building. What the trustees need to do is complete a simple application form at the municipality to inform them that there are more than 2 units in the building.

Lenroc Industries will supply a unit to an owner at no charge other than the installation fee of R495. The owner needs to sign a 5-year contract for the use of the system at a monthly charge of R 29,00 which contract must be renewed or continued on a monthly basis thereafter. This charge, which increases annually at CPI, is in respect of the vending company fees for handling the cash transactions, full maintenance of the unit and replacement in case of failure. The units will always remain the property of Lenroc Industries.

The occupier must only take responsibility for ensuring that batteries are replaced when required, to ensure continuing water flow.

Monthly management reports are available, which are programmed to include and highlight 'exception reporting.' An example of this is if someone should deliberately bypass the unit to avoid having to pay for water. The exception report will show zero consumption and it would be possible to investigate and take remedial action. Currently electricity meters do not have this benefit and bypassing is almost a daily occurrence. Naturally there may be penalties imposed by the body corporate for tampering or bypassing.

The meter is made of plastic alloy and has no recyclable value, unlike current normal water meters which are made of brass.

Thus far the suppliers have had an exceptionally positive response from property owners, bodies corporate, commercial and office building and developers of low cost housing. It is envisaged that with sufficient representation and exposure from Lenroc Industries that local authorities will in due course make it compulsory for all new buildings to have prepaid meters for single residential, group housing and bulk supplies for offices and small factories.

For further information, please contact Tony Bayley on 082.8881669 or e-mail him on tony@metersprepaid.co.za or visit www.metersprepaid.co.za

ABOUT TERTIUS MAREE ASSOCIATES

Tertius Maree Associates is a firm of attorneys based at Stellenbosch, specialising in the legal aspects related to the management and administration of sectional title schemes, home owners' associations, retirement and share block schemes and similar structures.

At Tertius Maree Associates we consult with and advise trustees, owners, managing agents, developers and attorneys, draft amendments and develop rules and constitutions, and have been doing so since 1994.

We also specialise in the recovery of arrear levies.

Tertius is the author of three books and approximately 800 articles on sectional title matters. In 1999 he obtained a master's degree in law (*cum laude*) at the University of Stellenbosch, focusing on sectional title law, and has served as part-time lecturer in sectional title law at that institution. He is also a proud honorary member of NAMA and a member of the development team of the STILUS levy insurance product for bodies corporate.

Tertius is ably assisted by two attorneys, Jacques Maree and Ilse Kotze, and a dedicated staff of long standing.

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